

P-3094/NA-92-534 ORDER FINDING UNAUTHORIZED OPERATION AND REQUIRING
REPORT ON CURRENT STATUS AND AVAILABLE REMEDIES

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

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Chair
Commissioner
Commissioner
Commissioner
Commissioner

In the Matter of a Request by Advanced
Communications Technology for a Certificate
of Authority to Resell Long Distance Services
in Minnesota

ISSUE DATE: March 23, 1994

DOCKET NO. P-3094/NA-92-534

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OPERATION AND REQUIRING REPORT
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PROCEDURAL HISTORY

On June 15, 1992, Advanced Communication Technologies Corporation (ACT or the Company) filed a petition requesting a certificate of authority to resell intrastate long distance services.

On May 6, 1993, the Minnesota Department of Public Service (the Department) filed its report and recommendation. The Department alleged that the Company had resold intrastate long distance services for three years in Minnesota before applying for authority to do so. The Department recommended that the Company be given a certificate of authority to resell long distance services only after paying penalties to the State of Minnesota for having provided intrastate long distance services without authority.

On May 20, 1993, ACT filed a letter explaining its delay in filing a request for authority. The Company stated that it had no knowledge that it was required to apply for a certificate of authority to conduct the business it has been conducting. Moreover, the Company denied that it resold intrastate services. The Company explained that, although it provided its increased discounts to AT&T intrastate usage, it did not charge its customers a fee for making those savings available.

On January 5, 1994, the Department filed an Addendum arguing that in light of the relevant statutes, Commission precedent and public policy, ACT and similar resellers are telecommunications carriers within the meaning of Minn. Stat. § 237.01, subd.6. As such ACT was required to obtain authorization from the Commission prior to furnishing such telephone service to the public.

On January 13, 1994, ACT filed a Memorandum responding to the Department's January 5, 1994 Addendum.

- First, the Company argued that "the certification issue" was moot because the Company no longer had any contractual obligations to AT&T or any other carrier and was merely an independent marketing agent.
- Second, the Company asserted that if the Commission found that the certification issue was not moot and proceeded to consider the Company's status the Commission should find that the Company has never been a telecommunications carrier under Minnesota statutes and, hence, that certification was never necessary.
- Finally, the Company asserted that, even if the Commission found that the Company was required to obtain a certificate of authority, its management fees were not discriminatory and no penalties were warranted.

On February 22, 1994, the Commission met to consider this matter.

FINDINGS AND CONCLUSIONS

A. ACT's Status is not a Moot Question

Contrary to ACT's assertion, the certification issues raised by the Department are not moot. The fact that the Company may have altered its status through a recent transaction with Enterprise Telecom Services, Inc. (ETS) certainly does not eliminate the question whether, prior to that time, ACT provided telecommunications service to the public in Minnesota with authority to do so.

Further, the Commission finds that the details of the post-transaction relationship between ETS and ACT have not been adequately developed to permit a determination of ACT's post-transaction status.¹ The Commission is not prepared, on the basis of this record, to find that the Company does not need a certificate of authority to conduct its post-transaction activities and that the transaction itself merits no further examination.

Accordingly, the Commission will proceed to examine ACT's pre-ETS transaction status in this Order and direct the Department to develop the record for future consideration of ACT's post-transaction status and the nature of the transaction itself.

B. ACT was Obligated to Obtain Authority to Operate in Minnesota at Least Prior to its Transaction With ETS

1. Nature of ACT's Pre-ETS Operations

In its June 15, 1993 petition, ACT referred to itself as a switchless reseller, which is a variety of telephone company or telecommunications carrier. In its January 15, 1994 memorandum, ACT reversed that definition and described itself as provider of consultive and network management

¹ The Commission uses the general term "transaction" to characterize the ACT-ETS arrangement because the exact nature of that arrangement is unclear. ACT has not provided the paperwork surrounding the deal. In its January 13, 1994 filing, the Company simply stated that ETS "absorbed" ACT's contracts with AT&T and provided the summary conclusion that the "transition" converted it into nothing more than an independent contractor.

services.

The Commission's jurisdiction is over the provision of intrastate telecommunications, including the resale of intrastate long distance service but not extending to consulting and management activities. Company-provided characterizations can be helpful but do not control. Even if the Company had consistently characterized its activities as resale or management, the Commission would examine the nature of the activity and judge for itself.

a. ACT Resold/Provided Intrastate Services to its Clients

In this case, examination of ACT's operation during the period in question shows that bundled under the term "management services" was the provision of telecommunications services, both intrastate services (subject to Commission jurisdiction) and interstate services (not subject to Commission jurisdiction).

The Company's claims and the circumstances that support the Commission's conclusion are as follows:

- The Company acknowledged that intrastate services were provided to its clients but denied that it (the Company) resold/provided those services.
- In addition, the Company minimized the significance of its intrastate traffic, estimating that its intrastate traffic comprised less than 10 percent of its business.
- Most important, according to the Company, the Company charges fees that are based solely on the clients' interstate usage, not the intrastate usage.

Purchased From AT&T

ACT denied the Department's characterization that the Company buys telephone service from AT&T. The Company asserted that it was simply like a guarantor of a loan, a status distinct from that of the purchaser. ACT stated that to conclude, as the Department did, that the Company was the actual purchaser of AT&T services is far-reaching.

The Company also denied that it sold (resold) telephone service to its clients. The Company characterized its activity as simply "enabling" its clients to take advantage of increased discounts from AT&T that they would normally be unable to receive on their own. In addition, the Company stated that it "passed on" the discounts for intrastate traffic. The Company denied that this "enabling" and "passing on" was "selling".

ACT's claim that its did not purchase telephone service from AT&T is unconvincing. In support of its claim, the Company emphasized that it never bought or purchased a block of time or service from AT&T "up front" (presumably meaning "in advance"). However, advance or prepayment is not a required characteristic of a purchase. Purchases are sometimes made with the agreement that payment will be made after the service or goods are supplied. The Company confirmed that its contract with AT&T called for this kind of payment, i.e. payment after supply. Regardless of when payment is agreed to be made, an agreement to pay for service is a purchase of that service.

Regarding the alleged lack of commitment to purchase a "block of time", this again is not required in order to make a transaction a purchase. However, it appears that the Company's contract with AT&T did indeed require "a minimum monthly usage" which is the functional equivalent of a commitment to purchase a block of time.

Finally, ACT denied that it could be classified as a purchaser because its client (the end-user) had primary financial responsibility for payment of AT&T bills. However, it acknowledged that its contract with AT&T obligated it to pay for the usage in the event that the client did not do so.

The Company's underlying obligation to pay for services used, an obligation required by AT&T as a prerequisite to providing the services in question, supports a finding that the Company, in effect, purchased those services from AT&T.

Resold to its Clients

ACT's attempt to distinguish what it said it did (provide its clients with larger discounts on AT&T intrastate services) from reselling/providing those services fails. The Company stood at the gateway to low rate AT&T services (more deeply discounted services) and charged its clients money to obtain access to telecommunications services at those rates. Those transactions are sales of telecommunications services.

Furthermore, the Company's denial of a link between payment of the management fee and the provision of AT&T *intrastate* service at the deep discounted rate is refuted by language in the Company's own Client Operating Agreement. The Agreement clearly states the link between payment of the "management" fee and access to intrastate service at discounted prices. The Agreement states in relevant part:

[The client] agrees to pay ACT a monthly management fee of \$ _____ for receiving the above listed discounts on its AT&T services.

The services "above-listed" in the Agreement include intrastate as well as interstate services.²

² The services include SDN outbound services such as "Dial 1" and Standard Megacom Wats and CSTP inbound 800 services.

Method of Calculating Fee Irrelevant

How the Company chose to calculate the amount of its fee is not relevant to this issue.³ The fact that the fee was calculated based on the level of *interstate service* consumed by the client is not relevant. If the Company calculated its fee on the basis of the market price of potatoes in Idaho, the fact remains that it exacted a price from the client for access to AT&T intrastate services. That exaction is a sale.

Percentage of Total Business Irrelevant

Though non-jurisdictional services may well constitute the large majority of the Company's activities, the fact is that for those activities that are subject to the Commission's jurisdiction (e.g. the provision of intrastate long distance service), it must abide by the requirements applicable to such activities.

Findings and Conclusion Regarding Resale/Provision Issue

Having examined the record in this matter, the Commission rejects the Company's characterization of its activities with respect to AT&T's intrastate long distance service. The Commission finds that, during the time period under consideration here, ACT contracted with AT&T to purchase interstate and intrastate long distance service in such a large amount that AT&T agreed to provide the service at a deep discount. ACT, in turn, contracted with clients who agreed to pay ACT "management fees" which entitled the client, among other things, to obtain intrastate long distance service from AT&T at the deep discount rate, a rate that the client would be unable to obtain by contracting directly with AT&T.

The Commission concludes that ACT's pre-ETS transaction activities included the resale of intrastate telecommunications service to the public. As the Commission has previously found, such resale constitutes the provision of telephone service.

b. ACT's Responsibility to Obtain a Certificate of Authority Prior to Providing Telecommunications Service to the Public

During the three years that ACT has been providing intrastate telecommunications service to the Minnesota public, as found above, the statutory framework has changed somewhat. However, the Company's obligation to obtain a certificate of authority from the Commission prior to providing telecommunications service to the public has remained constant.

³ Note: at issue at this point is simply whether the Company charged a fee for access to services including intrastate services. How the fee was calculated, however, will be very relevant to the issue of whether any of those fees were unreasonable, unfair or discriminatory. Consideration of that issue will occur elsewhere in this proceeding.

Period 1

Beginning with the commencement of its operation approximately three years ago and ending with August 1, 1993, the effective date of the "telecommunications carrier" statutes⁴, the statutes relevant to an analysis of ACT's operation and certification responsibilities were

- Minn. Stat. § 237.01, subd. 1 (1992) which defined telephone company in relevant part as any person, firm association or corporation furnishing any telephone service to the public and
- Minn. Stat. § 237.16, subd. 4 (1992) which prohibited telephone companies from operating any line, plant or system, or any extension thereof, or acquire ownership or control thereof, either directly or indirectly, without first obtaining a certificate of authority from the Commission.

Although ACT did not own any telephone equipment, it clearly acquired control thereof vis a vis its clients. The company stood at the gateway to the listed AT&T services at the reduced rates desired by ACT's clients. Through its Client Operating Agreement, the Company clearly established control over those services, requiring its clients to agree to the following:

ACT may terminate service if the Client's ACT invoices are ten (10) or more days past due.

This exercise of control over access to a telecommunications system is adequate under Minn. Stat. § 237.16, subd. 4 (1992) to obligate the Company to obtain a certificate of authority from the Commission before operating in this manner.

Period 2

Period 2 begins on August 1, 1993 and continues until ACT's change of status, if any, due to the ACT-ETS transaction mentioned earlier in this Order.

On August 1, 1993, an amendment to the definitions statute became effective. The amendment, Minn. Stat. § 237.01, subd. 6 (1993), removed a group of entities from the definition of telephone company and designated them "telecommunications carriers." The new statute defined "telecommunications carrier" as

a person, firm, association, or corporation authorized to furnish telephone service to the public other than

- entities authorized to furnish local exchange service,
- entities that derived more than 50 percent of their revenues from operator services provided to transient locations, and
- entities that provided centralized equal access services.

ACT met the definition of "telecommunications carrier" because as analyzed above it resold/provided (furnished) telecommunications service to the Minnesota public and did not meet any of the three exceptions listed above.

As a telecommunications carrier, ACT was subject to the certification provisions applicable to telecommunications carriers. In relevant part, Minn. Stat. § 237.74, subd. 12 (1993) prohibited

⁴ Minn. Stat. §§ 237.01, subd. 6 and 237.74, subd. 12 (1993), enacted by the legislature effective August 1, 1993.

any telecommunications carrier from operating or gaining control of any telecommunications system without first obtaining a certificate from the Commission. As found previously, ACT obtained that level of control through its arrangements with AT&T and its clients.

ACT's point that intrastate business only constituted a small fraction of its business is unavailing. Neither the definition of "telecommunications carrier" nor the statute requiring such entities to obtain a certificate of authority makes an exemption based on the proportion of intrastate versus interstate business the entity in question does.

Likewise, ACT's argument that the Commission lacks jurisdiction over the Company's intrastate long distance business because it only makes a profit on its interstate traffic is not relevant. The legislature did not insert a profitability factor into the definition of telecommunications carrier, nor did it exempt from the certification requirement telecommunications carriers that do not make or seek a profit from the intrastate service they provide.⁵

Period 3

Period 3 would begin on the date, if any, that ACT began to operate so differently that its regulatory obligations changed due to the transaction between ACT and ETS. That period, apparently, would continue to present.

The statutes applicable in Period 2 (the telecommunications carrier statutes) continued in effect following ACT's transaction with ETS. However, due to insufficient information in the record, the Commission is not prepared to determine what the Company's current status might be in light of those statutes.

To clarify this matter, the Commission will direct the Department to investigate the circumstances surrounding that transaction and the current status of the two companies (ACT and ETS) with respect to applicable statutes.

C. Summary of Commission Action

On the basis of the foregoing analysis, the Commission finds that at least prior to the December 29, 1993 transaction with ETS, ACT was a telephone service provider⁶. The Commission further finds that during the approximate three year period prior to the transaction with ETS, ACT provided intrastate long distance service without first obtaining a certificate of authority from the Commission to do so. Prior to August 1, 1993, this activity violated Minn. Stat. § 237.16, subd. 4 (1992). Beginning August 1, 1993, the effective date of the telecommunications carrier statutes, the activity violated Minn. Stat. § 237.74, subd. 12 (1993).

The Commission will direct the Department to file a report with the Commission presenting the full range of options available to the Commission to respond to the findings of unlawful activity made in this Order.

⁵ Even if there were such an exemption, it is not clear that the Company would qualify for it. The Commission looks to the substance over form. On paper, the Company may picture all its profit coming from activities beyond the Commission's jurisdiction (consulting and provision of interstate long distance service) but its provision of intrastate long distance at the low rates adds significant benefit to its total product and is likely maintained by the Company, not as an altruistic free benefit, but as a means of attracting paying clients. As such, the Company's provision of intrastate long distance service would be clearly intended as a profit generating activity.

⁶ The term telephone service provider used here encompasses "telephone company" [Minn. Stat. § 237.01, subd. 2 (1992)] and "telecommunications carrier" [Minn. Stat. § 237.01, subd 6, effective August 1, 1993].

In addition, the Commission will direct the Department to report on the current status of ACT in light of the ACT-ETS transaction. As part of its report, the Department should provide sufficient information to enable the Commission to determine whether ACT is currently a telephone service provider. The report should also examine the nature of the relationship between ACT and ETS and examine if a merger had occurred between the two companies in violation of any state law or Commission rule or policy.

For now, the Commission will defer for consideration in future proceedings the following questions: 1) whether ACT's rates have been unreasonably discriminatory, 2) whether ACT should be required, as the Department requested, to modify its tariff to describe specifically how the management fee is established, 3) whether penalties should be imposed, and 4) whether the Company's request for a certificate of authority to provide intrastate long distance service in Minnesota should be granted, denied or withdrawn.

ORDER

1. Within 45 days of this Order, the Minnesota Department of Public Service (the Department) shall file a report with the Commission which
 - a. presents the full range of options available to the Commission to respond to the findings of unlawful activity made in this Order;
 - b. addresses the Department's previous allegation that the Company's rates were unreasonably discriminatory in Periods 1 and 2⁷ and recommends an appropriate regulatory response to any such unreasonably discriminatory rates;
 - c. examines the current relationship between ACT and ETS and renders an opinion whether a merger has occurred between the two companies in violation of any state law or Commission rule or policy;
 - d. provides sufficient information to enable the Commission to determine whether ACT is currently a telephone service provider; gives the Department's view of the current status of ACT in light of the ACT-ETS transaction; and advises whether the Company needs to obtain a certificate of authority from the Commission for any of its current activity and what kind of tariffs or rates for its current activity it should file, if any; and
 - e. advises, in light of the circumstances, whether the Company's request for a certificate of authority to provide intrastate long distance service in Minnesota should be granted, denied, or withdrawn.
2. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)

⁷ Periods 1 and 2 are delineated in the text of this Order on pages 6 and 7.